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One Step Beyond:

Challenges and Opportunities in Promoting Quality Financial Services in Remoter Areas

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October 2002

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Executive Summary

Background

The last decade of microfinance practice, particularly in East Africa, has neglected rural finance. Support to the sector has concentrated on turning credit programmes into sustainable microfinance institutions (MFIs). This emphasis has produced a small number of MFIs that have either achieved financial sustainability or are close to achieving this. Their main product has been working capital loans provided through group-based lending methodologies. The result of this has been a focus on small-scale businesses and especially traders, who can manage these relatively inflexible products, and consequently also a concentration of their activities in urban environments and market centres. With outreach of between 150,000-200,000 they are, however, not yet reaching the bulk of poor Kenyans, most of whom live in rural areas.

At the same time there is evidence of innovation in Kenya in the form of managed ASCA programmes, Financial Service Associations and the emergence of 'non-traditional' SACCOs. While finance for agriculture remains a key challenge to the formal financial sector there is evidence from West Africa that some approaches to village banking based on community structures have achieved substantial coverage in rural areas, e.g. the MMD programme of Care in Niger which has reached approximately 400,000 women through low-level training and support to women's ASCAs. In addition, the experience of the Caisse Villageoises programme of CIDR and FECECAM in Mali also suggest that significant outreach and sustainability can be achieved in these contexts.

The purpose of this paper is therefore to:

- describe models of provision in Kenya that are reaching remoter areas or appear to have the potential to do so
- analyse the characteristics of these models
- present the outline of an action research project to promote rural financial service provision.

Reaching further out

Three models of provision are described and discussed:

- The ***managed ASCA*** model has outreach of approximately 30,000 in Central Kenya. Management services are provided to women's groups for a fee. Women save in groups of approximately 30 and take loans from the fund – an accumulating savings and credit association (ASCA). The products are short-term loans (at 10% per month) and longer-term loans of up to two years (at 17% flat per annum). The ASCA manager charges a fee based on the size of the overall loan fund. The managers travel to the groups once a month and help them run their operations. They also assist in following defaulters. The costs of this model are kept low because the managers use public transport, rent modest offices and employ diploma level staff.
- ***Financial Service Associations*** (FSAs) are a model that KDA has used to reach further into rural areas. Members buy shares, which are non-withdrawable and used for on-lending. The model also allows for a voluntary savings facility. Starting with at least 100 members the FSA elects a board, employs a locally recruited manager and cashier and commences lending. Interest rates of 10% per month help the fund to grow and costs to be covered. Salaries tend only to rise as the FSA is capable of paying. While the expectation was that once the system was set up and staff trained, the FSAs would be self-sustaining, this is only proving possible in a few cases and there is need for ongoing support. KDA is now examining models of provision of affordable support through management contracts and an apex option.
- ***Non-traditional SACCOs***. With SACCO liberalisation SACCOs are a convenient regulatory form that is increasingly being used to legitimise saving and on-lending. In some cases this is being used as an apex body for groups. Kieni Revolving Fund is such an example and services farmers and young people in the semi-arid division of Kieni, Nyeri District. However, non-traditional SACCOs are also emerging to serve small-scale traders and businesses. Ebony SACCO in Nakuru is of this form, but in this case has started to use groups because it found that individual lending with guarantors was problematic and group systems were able to better manage transactions and default.

Analysis and discussion

The common feature of these models is that they have elements of user-ownership. Community-based microfinance institutions (CBMFIs) are able to lower costs through the mobilisation of member's savings, retention of interest and profits, low overheads and voluntary inputs of labour into management and governance. In addition these systems are often more flexible and members have the ability to negotiate repayment schedules when problems strike, thus enabling them to more effectively manage livelihood shocks and vulnerability.

However, CBMFIs at the same time often suffer from poor management and governance. Where members are less well educated, the skills and experience to run these organisations effectively is often lacking and powerful members may manipulate them to individual advantage. Moreover, the more complex the products on offer, the more sophisticated the skills required for effective management and oversight. Hence, simple ROSCAs allow for transparent systems of management and oversight: all know what the payout is supposed to be, so that if it is not reached they know someone has not paid and action needs to be taken. Moreover, the end of a ROSCA cycle or ASCA termination acts as a transparency and control mechanism permitting problems to be addressed and reformation to take place under revised arrangements. The question arises as to whether it is possible to provide low cost support and supervision services to improve the management and governance of these types of organisation in order to improve rural provision.

The different models can also therefore be analysed in terms of the way they provide support services. The managed ASCA approach is one of private sector based consultancy on a fee for service basis, and this is a model with which KDA is experimenting as a means of providing long term support to FSAs. The question is how to balance the quality of the service and the price in a way that produces improvements in returns that will pay for the service and increase returns to shareholders.

The second model is that of a user-owned apex in which groups or FSAs pay a fee which might be based on either revenue or profits to fund the provision of a range of support services including training, support and supervision. Non-traditional SACCOs can also be conceived as apex bodies that are providing a structure of support service to groups. In this case the costs of the service are implicit in the interest on funds and fees charged.

Outline of an action research project

The opportunity exists to learn from these initiatives and attempt to address the challenges of management and governance through making available this experience along with toolkits aimed at improved management and governance. There are clear opportunities to improve the financial transparency of these models through the development of management information systems and standards. The project would therefore find ways of cost-effectively improving these systems and disseminating them to a wider audience that is also attempting to tackle rural finance provision. This would therefore aim to develop the broader infrastructure of support to CBMFIs.

The purpose of an action research project is therefore to improve the provision of quality demand-led financial services in rural areas and its specific objectives would be to:

(i) Research, analyse and document models of sustainable financial service provision that are reaching further into rural areas.

(ii) Improve the quality of affordable supervision and support services available to CBMFIs.Examine the implications of the different models of provision, support and supervision for regulation and supervision.

This would be achieved through working with a small number of main action research partners based in Kenya to generate improvements to their systems and how these perform. It would also seek to work with a wider network of partners in Kenya, Uganda and Tanzania to provide a forum for learning and dissemination on rural finance through a series of workshops. Organisations would be able to follow the developments in the project, test toolkits and present their own experience.

One Step Beyond:
Challenges and Opportunities in Promoting Quality Financial Services in Remoter Areas

Susan Johnson, Markku Malkamaki, Peter Mukwana and Kuria Wanjau

1. Background

The last decade of microfinance practice, particularly in East Africa, has neglected rural finance. Support to the sector has concentrated on turning credit programmes into sustainable microfinance institutions (MFIs). This emphasis has produced a small number of MFIs that have either achieved financial sustainability or are close to achieving this. In Kenya this includes organisations such as K-REP Bank, KWFT, Faulu-Africa, WEDCO and SMEP. These MFIs' main product has been working capital loans provided through group-based lending methodologies. The result of this has been a focus on small-scale businesses and especially traders, who can manage these relatively inflexible products, and consequently also a concentration of their activities in urban environments and market centres. While they are now beginning to develop new products the group-guaranteed, working-capital loan is still the core of their business. With outreach of between 150,000-200,000[1] these MFIs are however not yet reaching the bulk of poor Kenyans, most of who live in rural areas.

The provision of financial services in rural areas in Kenya has historically been the role of marketing co-operatives based on cash crops such as coffee, dairy and pyrethrum. With the gradual liberalisation of marketing systems and of co-operative legislation over the 1990s this sector has faced significant challenges. A major area of growth is the emergence of SACCO front offices services (FOSAs), which are moving into the space vacated by the formal sector banks. Banking sector liberalisation has resulted in many banks moving up market to target high net-worth customers and as a result their services have been put beyond the reach of poor people. At the same time SACCO liberalisation has resulted in new types of SACCO emerging, some based on 'check off' systems such as those in the tea industry and those based on transport associations (*matatus*, taxis etc). However other 'non-traditional' SACCOs are also emerging, some based in rural areas and acting as an apex for groups, as they offer a convenient regulatory format that allows for savings mobilisation as well as lending.

While microfinance is starting to find its way into the operations of other financial institutions, such as the Co-operative Bank, Equity Building Society and Family Finance, in being provided through a branch banking structure, provision is still mainly concentrated on towns.

There is evidence of extensive and increasing use of informal sector group mechanisms in Kenya (Johnson, 2002). Evidence from Central Province indicates that women regularly make use of merry-go-rounds (ROSCAs) with 45% participating in at least one and some using as many as five (Kimuyu, 1999; Johnson,2002). Moneylending is present and growing but relative to the volume of funds in informal sector groups appears to be much less important (Johnson, 2002).

At the same time there is evidence of in the form of managed ASCA programmes (Mule, Johnson et al., 2002) with some 27,000 women participating in them. These programmes involve a private company providing management services to women's group funds for a fee, so offering a more sophisticated set of services while at the same time offering the group greater confidence that the funds are being managed well. Similarly K-Rep Development Agency has been experimenting with Financial Service Associations (FSAs) as a means of providing financial services to remoter areas over the last 3-4 years.

While competition and innovation among the major MFI players and the emerging players in the banking sector is exciting, there nevertheless remains a question as to whether and to what extent these organisations will be able to reach remoter areas.

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[1] Estimates from AMFI.

By contrast, there is evidence from West Africa that some approaches to village banking based on community structures have achieved substantial coverage in rural areas, e.g. the MMD programme of Care in Niger which has reached approximately 400,000 women through low-level training and support to women's ASCAs[2]. In addition, the experience of the Caisse Villageoises programme of CIDR and FECECAM in Mali also suggest that significant outreach and sustainability can be achieved in these contexts[3].

The purpose of this paper is therefore to:

- describe models of provision in Kenya that are reaching remoter areas or appear to have the potential to do so
- analyse the characteristics of these models
- present the outline of an action research project to promote rural financial service provision.

2. Reaching further out: approaches to provision

For the purposes of the initial review that informs this paper the definition of remote or 'remoter' rural areas has been taken to be one where there is some evidence that the organisations concerned appear to be going at least 'one step beyond' the areas and types of clients with whom the mainstream MFIs have been working. This section describes three models that are in this sense reaching further out, but appearing to be doing so from a base that is inherently financially sustainable. The models are summarised in Table 1.

2.1 The managed ASCA model

This model evolved out of the withdrawal of donor support in 1993 from an NGO called Partnership for Productivity (PFP) (see Mule, Johnson et al., 2002 for a detailed discussion). PFP had been working with women's groups in a number of programmes from building water jars to saving. They decided to work with groups that had their own savings and developed a system for on lending both short term advances (called *gubasho*) for a month, and longer term loans for up to 24 months. After this system started working well key personnel from PFP decided to start their own organisations: the Women's Enterprise Development Institute (WEDI) and the Small Enterprise Development Institute (SEDI). Between them these organisations had an estimated outreach of 27,000 members in approximately 900 groups in 2001. The area covered stretched from Nyahururu to Kirinyaga with all three organisations having headquarter offices in Karatina.

Members make a minimum saving of Kshs100 per month and from the first month the funds are lent out. In these early months only short-term advances are given and they are returned with interest of 10% per month. When the fund has reached a sufficient size, usually after six months, longer term loans may be offered. These are given at 17% flat per annum and may run for up to 24 months.

At the end of the year dividends are paid depending on the interest generated by the fund and the shares held by each member. Evidence on dividends for 1999 suggested that they ranged from 15 – 60% although groups where default had reached problematic proportions did not receive a dividend and it was difficult to estimate the extent of these.

The organisations managing the ASCAs are fully financially sustainable. They keep costs low by renting offices, relying on public transport and employing staff who have bookkeeping skills or diplomas in business or commerce. New groups receive free service for three months and then pay a fee for each monthly meeting that is 1% of the value of the total revolving loan fund. This reaches a

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[2] Personal communication - Bill Grant, Ebony Consulting International, South Africa, September 2002

[3] See Chao-Beroff, R., T. H. H. Cao, et al. (2000). A comparative Analysis of Member-Based Microfinance Institutions in East and West Africa. Nairobi, ***MicroSave*** and Ouattara, K., G. T.-D. -. P. Nguyen, et al. (1997). The Caisses Villageoises D'Epargne et de Credit Autogerees in the Dogon Region of Mali: Elements of Impact. Ohio, CIDR/ Rural Finance Program, Ohio State University.

maximum of Kshs3,000 when the loan fund reaches Kshs300,000. The organisation sends an officer to the group meeting who organises the transactions and assists in follow up in cases of default.

Geographically the model has been centred on Central Province and has in the last two years extended to Nyahururu and Laikipia and Nakuru. Evidence suggests that the membership ranges from rural women farmers and petty traders to employees such as nurses and civil servants. The managers suggest that working in rural areas is easier than towns as these populations are more stable. However they are dependent on public transport and this constrains outreach. The furthest from the tarmac that they are able to reach is 25-30km. Indeed WEDI has recently opened an office in Nanyuki and is serving some groups who are 26km from the tarmac, regarding this as a test of whether they will be able to cover their costs.

The members in these groups report that they like the services because of the ease of access to loans; the flexibility of the loans, for example advances can be rolled over for up to 3 months and be taken for as little as Kshs500; the monthly structure which fits their activities better; the ability to re-negotiate the repayment schedule should genuine problems in repayment arise; the support they receive from the group at times of need[4]; and the dividends they receive at the end of the year. Many of these women feel that they could not cope with MFI loans even if they could access them.

The ASCA managers have faced serious challenges in managing default in recent years in the face of the national macroeconomic situation and are aware that it is in managing default that members assess their performance. With the growth of the model, which is now well known and resulting in many requests from groups for the organisations to come to assist them, the ASCA managers have not developed systems for reviewing the performance of groups or managing their staff. However the challenge is to develop their operations in a way that does not undermine the cost-effective system they have developed.

2.2 Financial Service Associations

K-Rep Development Agency (KDA) adopted this model of financial service provision in 1997 in a bid to reach areas that the main MFIs, including K-Rep Bank, were not reaching. The model involves community members buying shares in the FSA. These shares act as equity and are not withdrawable, however they can be sold on a willing buyer basis and may appreciate in value as retained earnings enhance the asset value of the FSA.

Members can borrow on the basis of their shareholding - usually up to a multiple of three times shares- and can purchase shares (base value Kshs300) as and when they wish. While initially loans involved guarantors who were also members of the FSA, default problems have resulted in the introduction of a group-based system of lending. Members wishing to borrow must now join a *Kikundi Cha Mpoko* (KCM) of five or six members and the group's collective savings are now held as collateral for the loan as well as the borrower's shares. Interest rates are 10% per month and loans are of variable term up to a maximum of two years.

The FSAs have also introduced current (*biashara)* savings accounts in which they can deposit any amount at any time with fees being paid on withdrawal. A range of other products including education (*masomo*) savings accounts and money transfer facilities are in operation in some of the FSAs.

Shareholders in the FSA elect a board, which in turn appoints a locally recruited manager and cashier. The original expectation was that after being set up and trained, the FSAs would become self-sustaining. Since managers and cashiers are paid by the FSA itself staff are usually paid according to the ability of the FSA. In the early days they may be paid very little, but even FSAs that are performing well are unlikely to pay their managers as much as the starting salary of a Credit Officer in an MFI.

[4] WEDI for example implements a model where there are welfare payouts from the fund in the event of a death in the immediate family. Kshs5000 to the family of a members; Kshs3000 for a spouse or child.

Costs are therefore kept low and the financial sustainability of the FSA is built into the model from the beginning.

Table 1: Summary of models

Model	**Managed ASCAs (WEDI, SEDI)**	**FSAs (KDA)**	**Non-traditional SACCOs (eg. Ebony, KIREFU)**
Membership	Approx. 30,000 in 1000 groups of approx. 30 members	Approx. 27,000 in FSAs with membership varying from 150-2000	These two SACCOs have memberships of approx 2000-3000.
Legal form	SHGs	SHGs	SACCO
Ownership	Members own shares in ASCA (withdrawable)	Members own shares (saleable but not withdrawable)	Members own shares (withdrawable)
Governance	Elected executive committee	Elected board	Elected board
Management	Private sector management service	Manager locally recruited - receive external support from KDA	Professional staff Both use group systems
Methodology	Monthly meetings at which members make savings and take loans	Members purchase shares in the FSA as and when they wish, against which they can borrow. A front office service for voluntary savings.	Members purchase shares in the SACCO with a minimum contribution per month and borrow against shares.
Services: - savings - loans	 Compulsory min./month Advances - 1 month Loans < 2 years	 Shares + voluntary savings Variable length to max 2 yrs	 Compulsory & developing voluntary services - community banks Most short term 3-12 months and max 2 years.
Outreach (cf MFIs) geographical socio-economic	 <30km from tarmac – constrained by public transport women farmers, housewives, petty traders	 Located in areas that MFIs were not reaching No evidence available	 Semi-arid areas (KIREFU) Ebony – adapting to groups own systems
Financial sustainability	Yes	FSAs - yes KDA services - no	Yes
Organisational sustainability	Yes	FSAs – show weaknesses in governance and management such that original "stand alone" intention only likely to be achieved by some FSAs	Yes
Key issues:	Managing default Improving MIS, internal control & audit systems	Not clear that FSAs can "stand alone" as originally envisaged. How to provide support services on a sustainable basis either through APEX or the market.	Ebony – flexible savings services through community banks demanded by members Kirefu – poor rains create default problems.

However, few FSAs have performed well enough to suggest that the model is likely to run effectively without ongoing external support. The turnover of board members and managers creates a constant demand for training and the need for ongoing support and supervision of their activities. Cases of fraud have also occurred and in some cases have only been revealed through KDA's audit system. Default problems have also severely damaged some FSAs with in some cases costly and time-consuming court proceedings continuing to damage their profitability.

So far KDA has provided training and support services free, but for the model to achieve long-term sustainability it is now necessary to find ways of providing this support in a financially sustainable way. As a result KDA is now considering alternative models of external support. The first is a management contract provided on a fee for service basis. The idea here is that providing higher quality management would lead to higher levels of performance in the FSA sufficient to pay for this service. An alternative approach is the creation of an Apex that would provide value added services to FSAs such as training, support and supervision to managers with the possibility that these services might extend to the intermediation of excess liquidity between FSAs.

2.3 Non-traditional SACCOs

Two non-traditional SACCOs were visited: Kieni Revolving Loan Fund (KIREFU) SACCO based in Nyeri and Ebony SACCO in Nakuru.

Kieni Revolving Fund (KIREFU)

Kirefu grew out of groups formed by IFAD to work on irrigation and agricultural projects on the Laikipia plateau. The chairman saw the need for the groups to be able to gain access to loans and conceived of a SACCO as a means through which the groups could pool savings and borrow. KIREFU was registered in 1995. The SACCO has some 3,800 members in approximately 200 groups and an outstanding loan fund of Kshs2m. However, due to recent droughts only some 100 groups are currently active. The system is structured on the nine locations in the division. Groups in each location elect a leader who is a management committee member. The locations also elect five delegates to form the locational credit committee and it is at this level that loan applications are reviewed and recommendations made.

Shares are Kshs50 and members make a minimum purchase of one share per month. There is also a Kshs5 contribution per share purchased for life insurance to cover loans should the member die. Loans are generally short term for four to six months because farmers are usually reliant on the sale of crops and hence they attempt to match the loan to the agricultural cycle. These are charged at 10% per month. Longer term loans for up to two years are charged at 15% per annum and it is proposed that 2% of this will be paid into the group's own funds as an incentive to collection. The group applies collectively to the SACCO for a loan that is then distributed to the group members.

In the past two years the area has experienced serious problems of drought and consequent repayment difficulties and cash flow problems. The SACCO employs an accountant and a training officer who does much of the field follow up. It has been able to contain its costs during this period by cutting back on sitting allowances of board members amongst other things, but the cashflow crisis has also affected the ability of the SACCO to lend and it has had to ration down applications to 1.5 times savings.

While the initiative is small and struggling within the context of agro-ecological conditions in Kieni, it is an example of how a non-traditional SACCO has arisen with SACCO liberalisation and operates as an apex body for self-help groups in a rural area.

<u>Ebony SACCO</u>

Ebony evolved from a self-help group of small-scale entrepreneurs who had been paying for business development services from a business consulting firm in Nakuru called Oakwood. The entrepreneurs faced constraints in implementing the advice they received because they lacked access to credit. Oakwood suggested that the entrepreneurs pooled savings and started to lend. It eventually registered as a SACCO in 1997. The SACCO now has 2,200 active members comprised of about 80 individual members and 74 groups, with a loan portfolio of approximately Kshs30m.

Initially the SACCO contracted Oakwood to manage it, but the SACCO now employs the manager direct. Its by-laws have been amended to allow three board positions to be appointed from non-members and these are approved by the AGM. The purpose is to provide a level of professional input to the board which members are often not able to give. The three professionals are from the fields of accounting, business development and law.

Members buy shares but decisions on lending to individual members are made at the group level. While it started with the usual individual membership structure, it found that guarantors would often abscond with the member and that this was system was not sufficiently strong to work with small-scale entrepreneurs and traders. The group is given an allocation of funds based on their collective shareholding and savings performance. The group knows that if a member does not repay then this jeopardises the access of other members of the group to loans. There are a number of loan products ranging from the *Akiba* loan which is based on the main SACCO loan product in which loans are up to three times savings and repaid over two years at 30% flat per annum. Additional products are shorter term loans: the *Mwireri* loan can be taken after saving for two months and eligibility is 3-4 times savings repayable between six and twelve months at 4% per month flat. In addition transactions loans are available to traders who need to fund a transaction taking less than a month. These are processed within two hours but for the member to access the facility s/he must first seek the agreement of the group. Transaction loans carry interest of 10% per month flat and *pro rata* if the funds are taken for less than a month.

This product range has been developed to cater to the needs of small-scale traders and business people who have to date formed Ebony's main clientele. However, it is gradually moving to serve groups who are on the outskirts of Nakuru and wish to do this in a way that will serve a much broader rural clientele. To do this they want to develop community banks that will allow for a more flexible range of savings services. Indeed, in one area the group members have already rented offices in preparation for a community bank to be run under a shared management arrangement with Ebony.

Hence while Ebony has yet to venture into the rural areas it presents the potential of doing so within a structure where the SACCO provides services to its members not only directly but also through shared the management arrangements with self-help groups.

3. Analysis and discussion

The previous section outlined models that are, or appear to have the potential to, reach further out into rural areas. They are all financially sustainable although they face challenges in terms of both financial and organisational sustainability. This section discusses these models further.

3.1 Lowering costs through user ownership and management

All of the models discussed above are user-owned. This allows costs to be reduced through a number of means. First, the savings of members are mobilised for on-lending at zero or negative financial cost Second, the interest charged can be retained in the fund in order to provide further funds for lending. If members do not receive dividends on their savings then of course they are receiving a negative return. However, it is important to note that the risks involved in putting savings into these systems may be lower than those of keeping savings in other places such as boxes at home (see Wright and Mutesasira, 2001). Therefore, even though these systems may offer only zero or negative returns they may be an improvement over the other options open to savers.

The second main way through which these systems reduce costs is because most community-based organisations (CBOs) operate entirely on the basis of volunteer management. SACCOs usually start out with voluntary management and graduate to employing staff full time when they have sufficient funds. FSAs operate in a similar way, with managers and cashiers receiving very low remuneration at the outset, but as the FSA generates more revenue it is usually able to pay the employees better. In addition because these staff are locally recruited these salaries may still provide an adequate income in these rural areas given the much lower cost of living.

Overheads are also kept low because operations can be run out of simple rented accommodation. Electricity might not be required or available as manual systems are used and operations mainly occur during the day. These organisations therefore start from a financially sustainable base and their costs only rise as they can afford to pay them.

The traditional rural SACCOs based around cash crops have been a major provider of credit to the agricultural sector in the past. Indeed it is both rural and urban SACCOs that are moving into the space that the commercial banks in Kenya have vacated through the development of front office services (FOSAs). However, while this is an area of new development that is likely to offer low cost banking services to poor people, it is less clear that these SACCOs are experimenting with alternative systems of outreach and coverage through for example, group-based systems. It is therefore rather interesting that the two SACCOs described briefly above that are operating with farmers and traders where there is no check-off system have found it necessary to operate using groups in order to lower costs and manage default.

In tackling provision in rural areas some banks offer mobile banking services. Indeed Equity Building Society in Kenya operates such a service. At present little is known about the outreach or viability of this service.

3.2 Advantages and disadvantages of user-owned systems

Research elsewhere suggests that there are a further set of reasons that user-owned or community-based microfinance institutions (CBMFIs) present important advantages to users.

First these organisations only survive if they respond to members needs for financial services. The fact that managed ASCAs allow women to take very small loans frequently responds to such a need. In these systems the 'feedback loop' (McCord, 2001) is direct. Members only join the groups if they respond to their needs and can also influence the group to provide the services that they require.

Second, interest rates are set by the members and interestingly they are often set quite high. As in the managed ASCA system, rates of 10% per month are not unusual although it is uncommon to find such high rates in SACCOs[5]. However, in contrast to the banks and other financial institutions members know that the rate will not change unless they have voted for it. Moreover because they receive the dividends they can set the interest rate high and benefit from high dividends also. Indeed, in the managed ASCA system, those who take advances at 10% per month had argued that they are contributing much more to the profits in the fund than those taking long-term loans at 17% per annum. As a result, the management agencies have adapted the calculation of the dividend and members now receive 10% of the interest they have paid on advances over the year as part of their dividend at the year-end – so that the effective rate they pay on the loans is 9% per month. This example shows how the system is responsive to the demands of users as well as emphasising the point that interest is not leaving the system.

One of the key reasons that users indicated that they like these systems is because they are able to renegotiate the repayment schedule when they face difficulties (see Johnson, 2002; Mule, Johnson et al., 2002). The ethos of these systems is that they are there for people to assist one another. In ASCAs and ROSCAs when a member has a repayment problem which is caused by what is regarded as a 'genuine' problem, the member can appeal to the committee to be allowed more time to repay. This flexibility

[5] While SACCOs and ASCAs are in many ways very similar, SACCOs (and FSAs) allow new entrants whereas ASCAs can restrict entry. The effect of restricting entry is that the value of the fund and earnings are not diluted by an increasing number of members and volume of shares. This effect means that returns are always likely to be higher in ASCAs and may contribute to the rationale in ASCAs for setting high interest rates since the dividends are not diluted.

means that members do not fear taking loans in these systems as they do in others, and unlike in MFI group solidarity systems the other members are not forced to make repayments on the member's behalf since they are being allowed to use the group's own funds for longer. In SACCOs the facility of emergency loans helps to accommodate these circumstances. In addition these systems also offer social support at times of need. Members may assist both financially and socially when problems strike. The social role of members is very significant and cannot be underestimated. For example, a death in the family means that the group or its representatives will attend the funeral.

However, it is the very nature of these advantages that also lead to the problems that user-owned systems face. The element of negotiability that these systems allow enables powerful individuals to manipulate them to their own advantage. These problems arise from a more general set of problems termed 'principal-agent problems' where the investors in the organisation – the shareholders - who are the principals, have to elect agents – board members – to represent and represent their interests that is they are given fiduciary responsibility. But when these organisations become large and it becomes harder for the members to monitor the performance of the board, they may in turn tend to protect their own interests and those of the management rather than those of the shareholders and the organisation. This can result in situations where board members arrange loans for themselves and managers arrange high salaries for themselves.

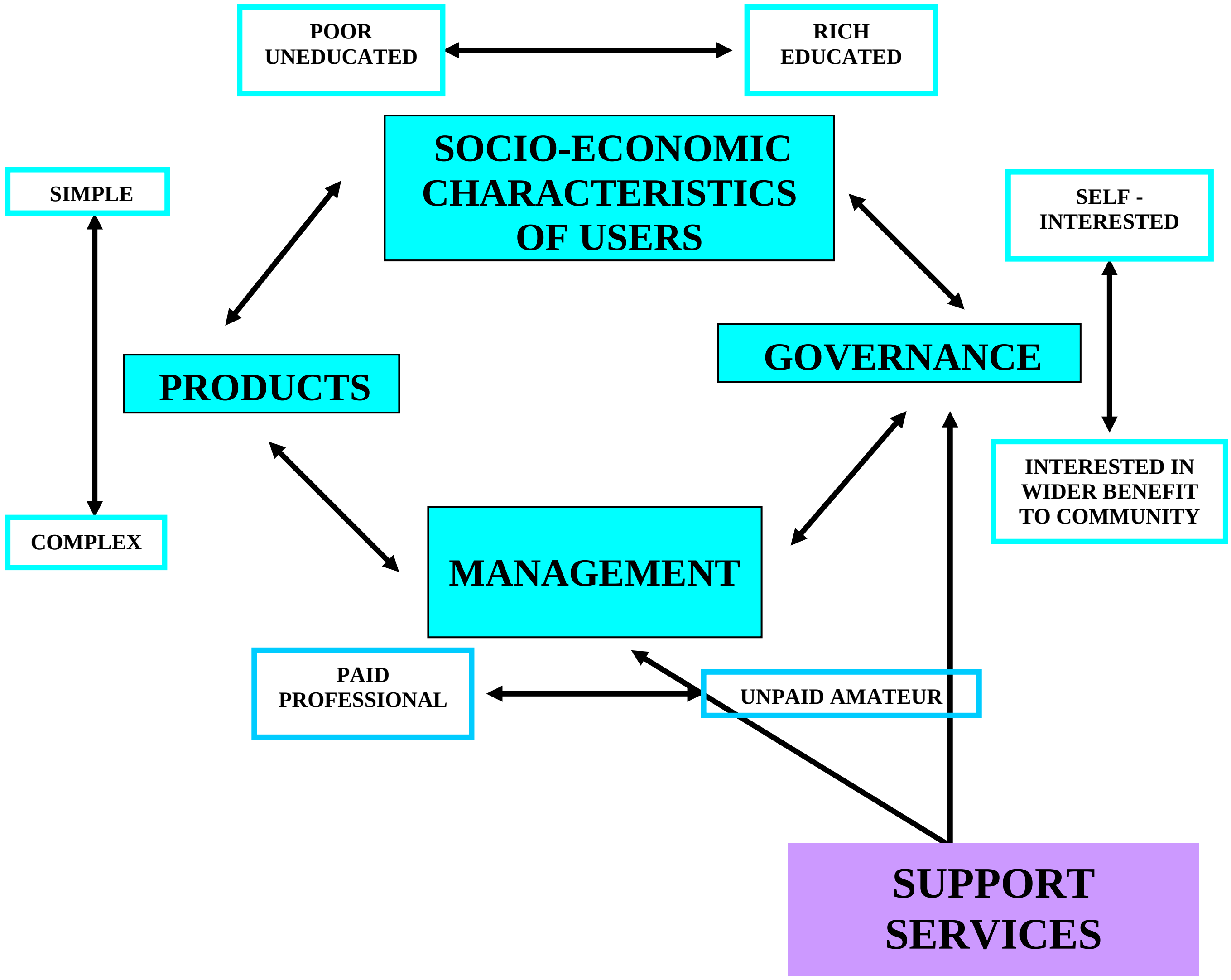
Figure 1 suggests how these problems become inter-related with socio-economic context and the range of products on offer. In a poorer and rural area the users of a system are likely to be poor and not well educated. The board of a SACCO or FSA is therefore elected from a group who may find it difficult to understand and monitor the performance of the management. The manager, may be in a powerful position to conceal information from the board, or vice versa the manager may be easily manipulated by members of the board who are operating in their own interests rather than those of the community. Poorly paid and amateur managers may find it difficult to manage the system. Indeed where these systems are most successful, it is often because there is a board member/s who are sufficiently disinterested and concerned with the benefit to the wider community and are sufficiently well qualified to supervise the management. Retired civil servants and professionals often play such a role and are significantly involved in supporting management.

When the products are complex, as for example in an FSA with both and loan and voluntary savings facilities, then the skills of the manager need to be stronger to deal with this and in turn the oversight required by the board is of a more sophisticated nature. At the opposite end of the spectrum, a ROSCA is such a simple mechanism that it makes the task of management and oversight very simple. All members know how much the payout from the group to a member should be and it is therefore simple to monitor this and all know that action needs to be taken if a member has not made their contribution. Moreover, the end of a ROSCA cycle, or termination of an ASCA, acts as a transparency and control mechanism permitting problems to be addressed and reformation to take place under revised arrangements.

Hence systems with simple products are also easier to manage and govern. Where the services provided are more complex, then the skills of managers and board members also have to be stronger to provide effective oversight. Indeed this is the problem that FSAs have tended to face: that the system presents challenges to the capabilities of many managers and boards leaving open the potential for fraud and manipulation by powerful members.

This is where support services have a role. It may be possible to provide services that can assist in addressing management and governance problems and improve the effectiveness of the system so also enhancing financial sustainability. The key question is the quality of such services and consequent price: the challenge is to get a combination of price and quality that improves the financial returns in the system sufficiently to generate the revenue to pay for the service.

Figure 1: User-owned systems – the inter-relation of elements



3.3 Affordable support services

An alternative way of examining the models reviewed above is to consider what approach they take to providing affordable support services to CBMFIs.

The first approach is the provision of private consultancy services on a fee for service basis. This is the approach that the managed ASCA model uses. The group is buying a service where a third party manages the fund in collaboration with the group. This improves the management input and is able to operate a more sophisticated system of loans (short and longer term, dividend payouts etc) as a result. In addition the ASCA manager assists in the follow up of defaulters. This is something that members appreciate because they often do not want to be seen as the people who are pursuing a friend, relative or neighbour. Hence it operates in the opposite way to an MFI group where the MFI uses the members to pursue the defaulter.

The management contracts for running FSAs with which KDA plans to experiment will operate on a similar fee for service basis. As indicated above, the key question is whether the managers brought in will be able to improve the performance of the FSAs sufficiently to be able to pay both for the service and improve the returns to the shareholders.

The second main approach is the provision of services through apex organisations. Member organisations usually pay a membership fee - in the case of the CVECAs in Mali this is based on a proportion of profits (Ouattara, Nguyen et al., 1997). In return they receive a range of support services such as training, auditing and conducting feasibility studies for new CVECAs. It is this model that KDA plans to experiment with in Taita Taveta where FSAs are keen to develop their own apex body.

An alternative approach to the formation of an apex is to create a SACCO in which members are either the groups or individuals within groups. It is this model that Kirefu adopted to form the apex body. In this case the interest and fees that the SACCO charges for its services cover costs of operating the apex organisation. Of course the degree of autonomy of the groups can differ substantially. In the case of Ebony, groups became the *modus operandi* in order to constrain default rather than it being formed as an apex for the groups themselves. However, anecdotal evidence suggests that with SACCO liberalisation other organisations working with a number of CBOs or self-help groups are looking at SACCOs as an appropriate form of apex organisation (for example the case of Saga in Western Kenya, Mugwanga, 2001) to enhance the sustainability of the groups into the longer term.

The key questions in terms of improving both the sustainability and quality of financial services in remoter areas are therefore:

- How to improve the quality of existing support services provided either by the private sector or through apex bodies and SACCOs?
- How to promote sustainable models of support services affordable to CBMFIs? And (to examine the implications of different approaches for regulation and supervision)What standards can be required in order to remove the need for central bank supervision?

4. Opportunities to address these challenges

The above review has suggested that a number of initiatives are in place that involve CBMFIs seeking to extend financial services further into rural areas. However, this has been a relatively neglected area for mainstream microfinance. Many development organisations working in rural areas have understood that previous NGO credit schemes have not been successful, but the main microfinance industry has not been actively working with them to find alternative means of improving supply in these areas.

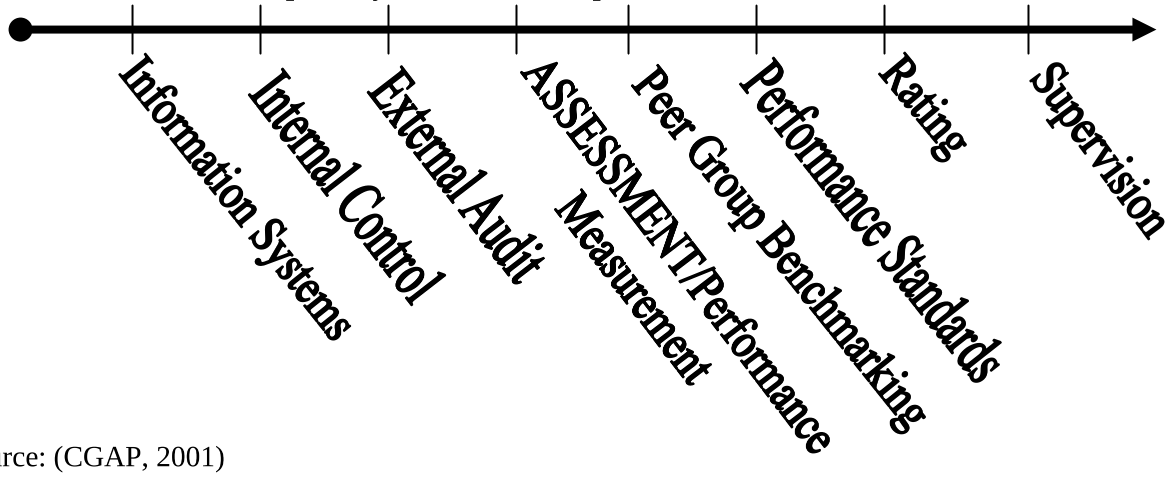
4.1 Opportunities for improving financial transparency

Improving the financial transparency of MFIs in the mainstream has been the focus of many of CGAP's efforts to develop the institutional infrastructure of the microfinance industry. The financial transparency information sequence shown in Figure 2 below demonstrates the steps through which the industry needs to move in order to develop its systems (CGAP, 2001). This process concerns the production, testing, dissemination and use of financial information. It starts with the gathering and reporting of accurate information (processes internal to the MFI), it then moves on to the verification of that information through systems of internal controls and then its external verification through external audit. The analysis, comparison and judging of the information are the next steps, finally resulting in MFI supervision to ensure that they comply with relevant standards.

Accordingly, it is possible to analyse the stage which the models reviewed in Section 2 above have reached in terms of financial transparency - see Table 2.

Thus the FSA model is producing internal financial information and has a system of internal controls such as the audit committee that oversees this process. In addition KDA has been conducting annual external audits of this information. While this information is consolidated at a wider level it has not yet been used to systematically assess performance or embark on the process of benchmarking appropriate performance for FSAs and developing standards out of this. If the FSAs are to become longer-term sustainable providers of financial services then it will be necessary to develop the infrastructure of services that surround them to this level.

Figure 2: Financial Transparency Information Sequence for MFIs



Source: (CGAP, 2001)

The ASCA management agencies produce information at the group level, but although their operations have expanded significantly in the last few years, none of them has yet developed improved systems of internal control over the officers who deal with the groups; internal audit of the finances of the groups; or management information systems which can enable group performance to be captured in ways that would improve management, monitoring and follow up. This is therefore something that these organisations need to develop if they are to be able to add value to their operations as they grow.

Non-traditional SACCOs have a choice of systems they can use. In some cases, the management information systems used by MFIs only need a little adaptation to deal with group-based systems within a SACCO structure. Equally the SACCO sector already has performance assessment systems such as Pearls that can be adapted to their needs. The concern here is to apply the existing approaches effectively and ensure that this is documented so that other non-traditional SACCOs can learn how to undertake these activities cost effectively.

At the level of independent ROSCAs and ASCAs there is scope for producing simple book-keeping systems which CBOs can adopt. In addition, it may be appropriate to develop a simple self-assessment tool so that groups can review their operations and consider how to improve them.

This analysis suggests that an action research project can add value to these existing systems by helping to upgrade the quality of their financial reporting and transparency. This can be done through a process of documenting models, identifying strengths and weaknesses that need to be addressed, and then developing toolkits with the organisations that can be used to test improved systems of information production and analysis.

Table 2: Opportunities for improving financial transparency of CBMFIs

Model	FSAs	Managed ASCAs	Non-traditional SACCOs	Independent ROSCAs/ ASCAs
Information systems	✔	Needed	Draw from MFI materials	Simple bookkeeping systems needed
Internal control	✔	Needed	Draw from MFI materials	Needed / Simplicity gives control
External audit	✔ (by KDA)	Needed	✔	N/A
Assessment/Performance measurement (including governance and management)	Needed		SACCO systems eg Pearls and similar to MFIs	Self-assessment tool
Peer group benchmarking	Needed		Similar to MFIs	
Performance standards	Needed			
Rating				
Supervision	Need to examine alternatives to central bank supervision.			
Potential outputs:	Toolkits for FSA operation Development of performance assessment and review standards	MIS & improved audit and control systems for ASCA managers. Toolkits for dissemination of the methodlogy	Promote toolkits for non-traditional SACCOs	Toolkits for running simple ROSCAs and ASCAs

4.2 Opportunities for improving governance and accountability

This approach does not only apply to financial systems. There is also an opportunity to address the concerns about management and governance identified above. Improvements in management and governance could be brought about by improving the training of boards on how to monitor management performance, for example through the provision of checklists and toolkits, and the training of members on how to monitor the performance of the group and board in similar ways. Improved means of making information transparent to poor people have been developed in a range of village based development programmes across the world that seek to ensure that local people are better informed about their rights in relation to government projects and service delivery. Alongside this, considerable work has also been done on organisational development of CBOs. There is therefore an opportunity to draw from this experience to improve the operation of CBOs that are providing financial services.

Hence outputs could include, for example, toolkits on governance for board members that could be used to train board members on how to interpret and monitor financial information being produced, this might include simple charts and diagrams which would allow the visual representation of key performance indicators at board meetings which would facilitate discussion. Equally for managed ASCAs, for example, a simple mechanism for improved transparency is the naming of defaulters at the meeting, the amounts outstanding and the reporting of follow up action being taken by the Executive Committee and the ASCA managers.

5. Outline of an Action Research Project

5.1 Purpose, outputs and activities of an action research project

An action research project would therefore have the purpose of improving the provision of quality demand-led financial services in rural areas through the following outputs and activities:

(i) Research, analyse and document models of sustainable financial service provision (both financially and organisationally) that are reaching further into rural areas.

The project would review the available literature on models of sustainable service provision in West and other parts of Africa that are reaching into rural areas and analyse the contributing factors. It will also identify and research models in Kenya that are reaching further out - whether community based or private provision - and document their achievements and challenges.

(ii) Improve the quality of affordable supervision and support services available to community-based MFIs.

It would work with three main action research partners to improve the quality of support services provided to CBMFIs. In particular to improve financial transparency and the accountability of management and governance structures. Working with:

- KDA to research and document alternative approaches to enhancing the organisational and financial sustainability of FSAs. KDA is experimenting with three alternative approaches:
    - Management contracts for FSA managers – their action research project aims to test whether improvements in performance through more professional management are affordable and therefore self-sustaining
    - Apex support to FSAs – whether the introduction of an apex body with a full time manager can provide value added services that will improve overall FSA performance
    - Social investment– whether the purchase of shares in the FSA by KREP as a social investor would lead to improved governance as a result of the exercise of voice in AGMs and the board.
- An ASCA management agency to improve the quality of service provision through increased transparency and accountability for management services and to develop cost-effective systems of monitoring performance.
- A non-traditional SACCO that operates with a group structure in order to identify mechanisms for management support to groups and shared management of community banks.

In addition it will seek to identify a small number of rurally based ROSCAs and ASCAS in order to devise improved book-keeping and self-assessment tools that can be used for wider dissemination.

(iii) Examine the implications of the different models of provision, support and supervision for regulation and supervision.Poor people face a range of risks when they place their savings in both informal and formal mechanisms. The project would aim to promote the financial transparency of these systems to members through improved governance and accountability. Where informal systems are more formalised and receive support services there is an opportunity to develop systems for oversight of these ASCA managers and support services either through self-regulation or through market based mechanisms, for example, basic grading or rating systems. The objective here is therefore to examine the implication of improved accountability and transparency to members for regulation and supervision, and to examine how systems of supervision can be provided without the direct involvement of the central bank in ways that can signal the relative risks of saving in different organisations to users.

For example, small user owned and managed systems (e.g. less than 100 members) may be required to make a declaration of risk, have their officers trained by certified trainers, have an annual simplified audit undertaken by certified auditors which are reviewed by members at their annual general meeting. Larger user-owned systems (e.g. more than 100 members) might be required to make a declaration of risk, have office holders trained by certified trainers, have a required reporting system subject to audit by certified auditors, and review their reports at the annual general meeting. In addition these organisations might belong to an umbrella body or apex, which periodically published performance tables which were reported in local media. (See Wright and Mutesasira, 2001).

5.2 Project methodology

This would involve two main components:

i. Work with three main action research partners in order to undertake detailed studies of their systems.

The approach involves the following steps:

- Review of literature on rural financial organisations and of toolkits available from these systems. A detailed review of 3-5 MFIs in Kenya (including the action research partners). This review will provide a baseline on the organisations visited and the action research partners in order to identify the means through which lower costs are being achieved and the financial and organisational sustainability of these approaches. The review will examine the:
    - The local social, economic and institutional context; the profile of clients using the services and their perceptions of the accountability and transparency of management and governance.
    - The financial systems in place, their strengths and weaknesses
    - The governance and management structures in place, their strengths and weaknesses.

  It will seek to identify the common challenges these models are facing and ensure that the outputs of the action research project have been appropriately identified.

- On the basis of the review a series of **draft toolkits** will be developed covering:
    - Governance: board and member education toolkits
    - Management: bookkeeping systems; internal controls; audit; management information systems; savings and credit methodology; portfolio and default management; legal issues for default and recovery management.
    - Reviewing CBMFIs: toolkits to review the above systems and organisational performance

- **Training and pilot implementation** of the draft toolkits with action research partners. This will involve a first round of training with partners to pilot test the toolkits aimed at improving the quality of their service provision.

- **Review of pilot test** of toolkits to examine how they are working and how they need to be adapted. This will involve engaging with clients, management and governance structures to establish whether and how the adoption of approaches in the toolkits have improved both organisational and financial transparency and accountability. A system of monitoring will be developed for this purpose that will also be available to other parties interested in testing the tools and approaches to make them applicable for different socio-cultural and economic environments.

- **Revisions and implementation of the toolkits**. The toolkits will be revised in the light of the findings of the review before being taken back to the organisations for implementation on a wider scale.

- **Final review.** A final review of the impact of the toolkits and improved systems will be undertaken before toolkits are finalised.

ii. ***The project will also work with a wider group of stakeholders who demonstrate interest in the project and wish to be involved.*** An initial workshop held in Nairobi in September 2002 suggests that there are many organisations– including in Uganda and Tanzania - who wish to engage with this initiative. This engagement will primarily occur through a series of six-monthly workshops that will create a forum for dissemination and learning on rural finance in East Africa. Stakeholders will be able to follow the progress of work with the main action research partners, to adopt toolkits for their own use and use the workshops to present their own experience. The workshops will also bring in experiences from West Africa for discussion and dissemination.

Workshop 1: review of existing toolkits, and re-working of draft toolkits prepared by ***MicroSave*** for the project. Organisations and networks which have already developed toolkits and systems to assist with the management, support and supervision of CBMFIs will be invited to work with the ***MicroSave*** team to finalise the draft toolkits.
Workshop 2: dissemination of baseline review of organisations and draft toolkits. Organisations who wish to use the toolkits will be encouraged to do so using a similar monitoring system to that used with the main action research partners.
Workshop 3: dissemination of findings from toolkits review with main partners and presentations from other organisations testing the toolkits.
Workshop 4: focusing on presentations from other projects, their experiences and issues arising.
Workshop 5: final workshop to present findings of work with action research partners and experiences of other stakeholders.

5.3 Project outputs

These would be a series of research reports and the toolkits indicated above, as follows:

- ***First research report*** to be produced in collaboration with KDA presenting a baseline review of FSAs in preparation for the testing of management contracts and an apex approach. "Achievements and challenges of FSAs in Kenya: a baseline report"
- ***Second research report*** documenting findings of the baseline review of literature and 3-5 detailed reviews of MFIs in Kenya: "One Step Beyond: achievements and challenges in reaching remoter areas".
- ***Draft toolkits*** ready for testing and limited dissemination to interested stakeholders. The toolkits are as listed above covering Governance, Management and Reviewing CBMFIs.
- ***Third research report***: "Improving the quality of services provided by CBMFIs: an interim review". This will document the findings of the interim review of pilot testing of the draft toolkits.
- ***Fourth research report*** in collaboration with KDA will present interim findings on progress with the alternative support systems of management contracts. "Alternative support systems for FSAs: an interim report"
- ***Fifth research report***: "Beyond supervision: enhancing transparency and supervision of rural finance organisations". This report will consider the implications of the different support and supervision models in relation to legal and regulatory frameworks.
- ***Final research report*** documenting the experience of the project in working with action research partners: "Improving the quality of services provided by CBMFIs: experience from an action research project"
- ***Toolkits*** on management, governance and reviewing CBMFIs finalised and published.

6. Conclusions

Rural finance in East Africa has been neglected by the microfinance industry for the last decade. Over this period there have also been fundamental changes in the availability of services through the banks, parastatal financial institutions and traditional SACCOs as liberalisation and restructuring have reduced the extent of provision.

Experience in West Africa suggests that community-based systems have been able to significantly extend outreach to the rural areas. There is evidence that such systems are also gaining ground in East Africa. Community-based MFIs offer the prospect of expanding provision because of their lower cost structures, but present challenges in terms of the quality of governance and management.

The analysis of approaches given here suggests that there are clear opportunities to improve the transparency and accountability of existing systems through the development of the infrastructure of the industry by finding means of applying similar principles as have been applied to mainstream MFIs but simplifying them and making them appropriate to these systems. This challenge of affordability is critical.

The proposal here then is for an action research project that would develop and experiment with improved systems of governance and accountability with a small number of action research partners, while developing a forum for the discussion of rural finance experience in East Africa more generally.

Annex 1: One Step Beyond: Proceedings of a workshop held at the Fairview Hotel, 20th September 2002.

In order to plan the project outlined in the latter parts of this paper, ***MicroSave*** sought inputs other microfinance actors in a workshop held in Nairobi. (See enclosed agenda and the list of participants).

The purposes of the workshop were: (i) to consult other players in the design of the research framework; and (ii) to identify potential stakeholders and their potential roles in such a project.

The objective of the morning session was to identify the key challenges that are facing institutions that are trying to go 'one step beyond' the traditional MFI's.
The objective of the afternoon session was to discuss how ***MicroSave*** Action Research might tackle these challenges.

1. Key challenges facing organisations trying to go 'One Step Beyond'

Based on Susan Johnson's presentation the participants were divided into breakout groups that discussed the following questions:

1.What other models of sustainable financial provisions in remoter rural areas exist besides Financial Services Associations, Managed ASCAs and non-traditional SACCOs?
2.What makes these systems low cost?
3.What makes them un-sustainable?
4. What other models of affordable and sustainable support services to CBMFIs exist?
5.What are the key issues in improving governance of CBMFIs?
6.What are the key issues in improving management?
– where self managed
– where management provided on a fee for service basis
7. What forms of external quality control of these organisations might exist without involving Central Bank direct supervision and regulation?

Feedback from break out groups was as follows:

What other models of sustainable financial provisions in remoter rural areas exist?

The groups gave the following as other models that are competing favourably with MFIs:

- Non-traditional SACCOs like Ebony SACCO in Nakuru is trying to develop Community Banks. Ebony plans to provide support and supervision services. These are owned, serve and are managed by the local community. Ebony will give an oversight service. Ebony had found that the link between managers and members was weak – now finding ways of improving the communication. Ebony has also Co-opted members onto board to improve governance.
- In China, there was a mobile agent based system where the agent was paid a commission to give service to members, served about 35,000 clients under the Agricultural Bank of China. Financial sustainability was attained through low agent costs at 3% which also covered the bookkeeping (this was kept simple), cost of funds was also low/zero/negative. Agents required random monitoring. The agents were appointed by the villagers they served hence had a strong attachment and understanding of the village. Agents only had primary school education which meant they were cheaper to hire but this came with high levels of numeracy. The Villages were relatively stable and 80% of the villagers used the service which meant that diverse needs were addressed.
- Linkage banking model. This links self-help groups (SHGs) to banks where banks issue individual loans using group funds as collateral. The SHGs manage liquidity within groups by accessing funds from the banks. In Uganda/Tanzania rural SACCOs with excess liquidity can use it for group lending to SHGs with liquidity problems. This can be done through Co-operative Apexes and Banks, which then provide liquidity intermediation.

- FISEDA in Tanzania is promoting new community based SACCOs and avoiding old ones in a bid to start out right. So far 5 new ones have been formed. They are based on a ward which comprises 5-7 villages. A village has a sub-committee/group to work at the village level. They act as volunteer savings collectors, and recommend loans. (User-involvement at this level)
- Some Financial Services Associations (FSAs) have been set up by a trust of professional local people who are based in Nairobi. Mainly depend on trust for rapid development. The trust also performs audits and provides manpower to FSAs since it comprises professionals with skills and pro bono local philanthropists. Depends on communities that are relatively developed and have sent people out to be educated and have experience with which they return. Other FSA models e.g. FSAI in Uganda where 10% of gross revenue is charged for supervision. Sustainability is still a question because of the heavy technical support they are currently getting. This approach is operating a type of franchise with strong branding. Kenyan FSAs have more diversity and this makes it more difficult to provide a consolidated support and supervision service
- In Tanzania, a traditional MFI hired agents from the local community to do loan appraisal, disbursements etc – paid on commission. It experienced problems of MIS and delinquency because agents approve many loans so as to gain in commissions. Had a deep reach because of the agent's low cost structure. Model collapsed for unknown reasons. Moneylenders (shylocks). Low cost because they are one man shows, no book keeping, clients come to the lender to borrow/repay; they also have no social welfare so are more aggressive in collection, have client knowledge, attract clients because money is accessible in large amounts and is always available and mainly deal with traders hence the repayment is better. Recover interest up front hence earnings are boosted.
- Aga Khan Foundation Rural Support Programme – Kenyan Coast: Kwale, Kilifi. More information on how this works is needed. Saga in Nyanza. This is a community focused private company, which works with ASCAs and has formed itself like a SACCO apex. Each ASCA uses SAGA's service centre at a fee to cover Head Office and Service centre operations. Uses link bank to carry out some of its services.Accumulating Savings groups based on extended family or clan (can have over 1000 members)
- Traditional SACCOs are changing e.g.Upimajinaramani in Mbeya, Babati teachers with about 150 members; both are extending services.
- Young men's (teenage) savings clubs for the purpose of entertainment
- Well-to-do persons in the village lend money in exchange for maize or cows
- Merry-go-round in the asset form e.g. cows or services like book keeping services, healthcare, consultancy services like on water development etc. Offer voluntary services hence low cost. Groups are coming in to fill the void left by BDAs.
- Supplier credit where groups guarantee members for supply of merchandise.
- Saving with traders

What makes these systems low cost?

- Shared values
- Exploiting pre-existing trust: where members feel that it is not worth defaulting since they all know and relate with each other.
- Information is cheap mainly through reputation and past events or performance: defaulters are therefore screened out easily. The group is composed of people who have been brought together by "good mannerism"
- Use the pre-existing structures which are simple. The groups do not therefore incur any costs to set up the structures.
- FSAs: Every member is given a record of their activities with the FSA after every transaction to enhance transparency. The execution of a transaction needs two people for internal control. FSAs cut down costs by reducing opening times.
- KWFT members use services of the FSAs in the same area e.g to bank cheques and save in the FSA.

What are the key issues in improving management of CBMFIs?

- Try to use existing structures at the community level.
- The community should suggest the improvements. Member education – Group leaders present to other groups
  - –FISEDA – training members on key questions to ask and key data.
  - –Institutional things to do – separate audit committee from executive committee
  - –Audit committee not on the board.
  - –How to provide support services for governance at affordable rates – offer advice.
  - –SACCO movement – too many providers of the same support services and no co-ordination.
  - -There has been lots of training but no supervision and follow up.
- Lots of opportunities to use existing training modules rather than re-inventing the wheel!
- Establish standards and indicators that can be used to rate institutions and groups, both externally and between peers (e.g.1 star to 5 star).
- Controls/audits - (audits should cover more than the books- management audits)
- Improve guidance on election procedures
- Supervision/external supervision – use of an apex.
- Clear and shared mission
- Profitability for organizations to support apex activities.
- Improving transparency
- Encourage Ownership at grass root level.
- Efficiency and effectiveness of the apex to provide the services.
- Apex to engage in fee-paying services.
- Ability of the apex to deal with industry wide issues (e.g promotion of common standards) instead of management/ operational issues e.g. developing manualsSelection & Qualification, remuneration, supervision, in-Service training, empowering Information Systems

What are the key issues in improving governance of CBMFIs?

- Develop self-regulatory mechanisms and create legal mandate to enforce – done by contract.
- More donor involvement in governance of partner organizations –to be part of the performance standards.
- Clear policies and procedures including systems – ensure these are enforced.
- Capacity building of management staff.
- Standardization of services
- Strengthen By-Laws eg Board selection criteria How to rate externally - 1 star to 5 star outfits?

What forms of external quality control of these organisations might exist without involving Central Bank direct supervision and regulation?

- Rating agencies – use standards to rate. The rating should be consequential.
- Apex organization to provide 2nd tier quality control services.
- Umbrella/Apex Organizations Self-assessment mechanism within organizations.
- Peer reviews.

2. Planning The Action Research Project

The objective of the afternoon session was to discuss how ***MicroSave*** might design its ‘One Step Beyond’ Action Research Project. The purpose of this session was also to identify potential stakeholders and their roles for this project.

Based on Markku Malkamäki’s presentation the participants were divided into breakout groups that discussed the following questions:

1.How should we work with

- core action research partners?
- how should we work with other interested parties?

2.What other outputs are needed?
3.What other projects are addressing similar issues?
4.What other financial institutions should be included? In Kenya? In Eastern Africa? In Africa as a whole?
6.What other networks should we work with?
7.What kind of dissemination of the results/toolkits is most appropriate?

How should we work with core action research partners?

- Develop clear guidelines on how to work with ARPs. Identify the contact person in each of the partner institution.
- Meeting with the partners to clearly define the objectives and outputs of the partnership
- Identify the roles of collaborating partners
- Draw an action plan
- Ensure ARPs buy-in to the idea, because management and governance are very sensitive issues
- In order to eventually disseminate the research findings, the project should work with systems where available by dealing with institutions e.g. apexes, consultants, local audit firms, colleges, specialized IT consultants and management training providers. This will help in distributing toolkits to the system rather than benefit a few institutions.
- Consulting mode/workshop mode/toolkit mode: find the right mix when working with partners
- If one size fits all, it can become useless
- Making explicit what is the role of ***MicroSave*** (not a donor and not just a consultant)

How should we work with other interested parties?

- Involve AMFI, AFRACA, KUSCCO, KERUSSU etc in regulatory discussions about rural finance
- Need to identify other key organisations that might want to test out the tools along the way in Uganda and Tanzania: DFID could assist with monitoring systems.Come up with criteria of selecting the partners
- Based on the criteria above, identify the partners
- Follow process given above (under Core Partners)
- Consider involving traditional SACCOs who are not necessarily as hide bound as is usually the case.Implement the toolkits; ensure quality control of training and follow up for feedback after dissemination.

What other outputs are needed?

- Do a comparative research study to look at the sustainability of the alternative models including outreach. Also compare with more structured, non-user owned models reaching out further e.g. Equity. Example given where a private company has been giving services to rural areas for purchase of solar panels. How does it reach down?
- Comparative study of successes and failures within a system/model and if possible between systems.
- Do a comparative study of products among the different models
- Need to look at bigger traditional SACCOs that are trying to change – all they know is seasonal input lending. They need to know about how to serve different markets. For example, many are starting FOSAs – how to adapt ***MicroSave*** tools to their use? This will be an opportunity to add value to the traditional SACCO sector. They feel left out of what is happening in Microfinance sector
- Development of a policy framework since there lacks a rural finance policy that addresses implications of regulation and supervision. Involve the Apexes in this. This will involve coming up with recommendations on appropriate legal structures in which different forms of

intervention can be addressed.Develop case-studies (low cost digital video) on working with an action research partner
- Different modes of disseminating toolkits and findings including how to disseminate these outside Kenya e.g. low-cost digital video, briefing notes, cross-visits (eg. one FSA visiting another)
- MIS-guidance toolkit

What other projects are addressing similar issues?
- Consider results/outputs from WOCCU-Kenya project, AFRACA
- CIDR and Freedom from Hunger women groups program in West Africa.
- Cameroonian experience in "Njangi"
- WOCCU-Uganda project.
- CARE International – MMD project
- SHDF program in Zimbabwe
- FAO literature
- DFID working with FSAs in Uganda & Tanzania also with DID, FESEDA, etc.
- Africa Now – very small SACCOs
- AKRSP – VDOs with SACCO as an APEX
- Tanzania – RUFIP (Rural Finance Development Project) – In Mwanza & Mara regions: They look at Institutions reaching rural areas, their operations, standards, transparency, etc.SCC is developing a project with village-based SACCO
- Co-op Bank training small scale MFIs

What other financial institutions should be included? In Kenya? In Eastern Africa? In the whole Africa?
- Co-op Bank in Kenya;
- FSA Intl
- Cameroon – MC2s? Guinea – FSAs.
- VISACAs Gambia?
- Guinea – rural finance…?
- Caisse Villageoises –DID now replicating in TZ
- Africa Now
- Aga Khan Foundation
- Wedco
- FINCA – Uganda/Tanzania
- CRS?
- CRDB
- Programs in French speaking in West Africa have successful training, governance and bookkeeping materials. Credit Rural de Guinee is one. IRAM, Desjardins

What other networks should we work with?
- WOCCU
- AMFI
- ICA- International Cooperative Alliance
- INAFI
- AFRACA
- KERUSSU?
- AMFIU
- Tanzania – SCCULT; Uganda – UCA; USCU

How other networks should be involved?
- Define levels of involvement for all institutions e.g. asking an institution like WOCCU to evaluate the toolkits.
- Involve them in the initial/planning stage

- Research stage – Experts in particular areas to be contracted to deliver based on ***MicroSave****'s* Terms of reference.
- Toolkit testing phase
- Dissemination stage
- Studies collaboration – at information exchange level

What other reports are needed?

- Reports highlighting the differences in the MFIs before and after using the toolkits.
- Want to know whether the institutions are making money – how to make it cost effective?
- How to pay for supervision/oversight services.
- Comparison of product pricing between different models – are shares really appreciating.
- Reports on their delivery systems
- Reports on performance & challenges
- Their strategies to overcome their challenges (mainly governance & management)

What kind of dissemination of the results/toolkits is most appropriate?

- Appoint a partner in each of the other countries for second tier testing and feedback.
- Dissemination by partners themselves
- Periodic workshops – say one 2-days workshop every six months.
- Put draft toolkits on website with health warnings! And monitoring tools.
- Publications
- Through networks even in different countries
- Briefing notes i.e. ***MicroSave*** style
- Digital videos on a CD
- Visits
- Radio

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